

# How 2 Guys Iowa Connection Took Big Telecoms for a Ride

**Calls Sent to Their Area  
Piled Up Access Fees  
Until FCC Interceded**

By **DIONNE SEARCEY**  
*October 4, 2007; Page A1*

RICEVILLE, Iowa -- Two-and-a-half years ago Ron Laudner was the anxious owner of a rural phone company serving this tiny town, where Main Street was emptying out as restaurants and other businesses disconnected their phones and moved to busier commercial districts.

More than 1,800 miles away, David Erickson was running a Web-based conference-calling business in Long Beach, Calif., shopping around for phone companies to be his partners.



**Ron Laudner**



**David Erickson**

In mid-summer 2005 this unlikely duo struck a deal. They routed millions of minutes of Mr. Erickson's conference calls through the switches of Mr. Laudner's Farmers Telephone of Riceville. To do it, they used outdated federal regulations to charge telecom companies such as **AT&T Inc.** and **Verizon Communications Inc.** steep rates and collected huge profits at their expense. Together, the two made hundreds of thousands of dollars. Soon, Mr. Laudner cut other deals to generate even more traffic. At the peak, his little telephone company was facilitating conversations among everybody from Mary Kay Cosmetics employees to customers of Male Box, an "all male all gay" chat line.

"I'm not going to argue I didn't think it was amazing," Mr. Laudner says.

But the big phone companies had another term for it. "Verizon is not going to stand by while irresponsible companies use this traffic-pumping scheme to overcharge our company," says Tom Tauke, vice president of public affairs, policy and communications for Verizon.

The deal between Messrs. Laudner and Erickson illustrates how tumult in the telecom industry has given rise to opportunities -- and headaches -- as entrepreneurs exploit outdated regulation. Their arrangement, and deals like it, spawned lawsuits, blocked phone calls and triggered an investigation by the U.S. Federal Communications Commission into the high fees some rural carriers charged to the Bells. Late Tuesday, the FCC proposed rules that, if approved, are likely to prevent such deals in the future.

"We got smacked and smacked hard," Mr. Laudner says.

The partnerships benefited from the confluence of hot demand for conference calling and a proliferation of cheap long-distance plans. But the key was federal rules drafted during the 1983 break-up of Ma Bell, which required big telecom companies to pay hefty fees to small carriers to compensate for the high cost of providing service across miles of sparse farmland. Today, because of new technology, hundreds of callers can be linked at very little cost, no matter their location.

The Iowa plan worked like this: Mr. Erickson's freeconferencecall.com assigned a local Iowa telephone number to a group offering a conference call. When customers dialed the number, they went through their own carriers -- say, AT&T -- to be routed to Farmers Telephone in Iowa. Farmers Telephone then linked the callers to each other. Farmers charged the Bells steep rates to transmit their customers' calls and split the proceeds with freeconferencecall.com.

Mr. Erickson is a 42-year-old high-school graduate from Long Beach who gave up a childhood dream of becoming an architect to instead run construction companies that built machines for designing curbs and gutters. He dabbled in running insurance companies briefly before getting interested in telecom by going to a trade show with a friend and being wowed by a device that allows videoconferencing between PCs.

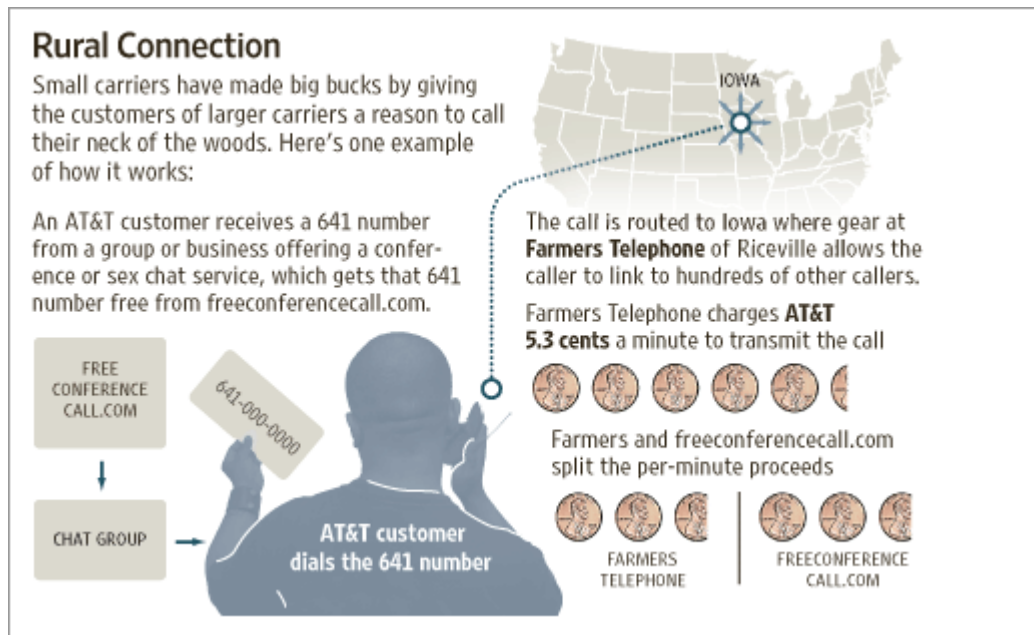
Mr. Erickson formed freeconferencecall.com in October 2001 working with a Boston phone company. He handled the marketing to attract customers to the service while the phone company provided the phone numbers and transmitted the calls. Mr. Erickson's business plan was to give away free conference calling and sell businesses other things, like a service that would allow users in multiple locations to work on spreadsheets simultaneously.

Other startups were doing the same thing, many of them depending on customers looking for sex chats. These customers have flocked to the free conference-call startups rather than pay costly fees associated with the 900-number sex industry, which has shrunk dramatically with the advent of inexpensive Internet-calling options and Internet-based pornography.

Mr. Erickson says he doesn't market to sex chat groups, but concedes he can't control who uses his free calling service.

Mr. Erickson realized early on there was money to be made from sharing the revenue that his phone-company partners were able to collect from the major carriers. Back in 2001, he started researching the fees and not long after recognized that rural phone companies, which could charge the Bells significantly higher fees than those in urban areas, presented an opportunity.

Mr. Laudner, a robust 49-year-old who has spiky gray hair, a goatee and an earring, was born in an apartment over a phone office his father managed in nearby Rudd, Iowa. One of his first jobs was driving through the cornfield-lined countryside in 1974 for a local



phone company replacing customers' rotary-dial phones with more modern touch-tone phones. In 1995 he took over Farmers Telephone and two other rural phone companies all created in the early 1900s when isolated farmers strung wires along fences to get phone service.

In recent years, Mr. Laudner has been eager to find ways to compensate for his shrinking core business, land-line phones. He created a slogan, "Let's talk," and participated in a dozen parades through neighboring towns, decorating his company's float to resemble an iPod to reflect new consumer technologies. He dreamed of rallying his Iowa phone company friends to help build a wireless business in rural Iraq but decided the country became too violent to safely set up shop.

In the spring of 2005, Mr. Laudner bought gear to help him market new Internet-based phone services such as Internet calling, video services, conference calling and other services to businesses outside Riceville's shrinking Main Street. A consultant, Darin Rohead, who helped sell him the equipment, put Mr. Erickson and Mr. Laudner in touch. Over a phone call they soon struck a deal, with Mr. Erickson mailing him gear to install that would enable the calls.

"I'll make you as successful as you want to be," Mr. Laudner remembers Mr. Erickson telling him.

Mr. Laudner offered the firm phone numbers with the local 641 area code to use to market free conference calls and other services. Callers who dialed the 641 number

would pay the long-distance charge, which is now close to free in many plans. They would then be linked to one another through telecom gear in Mr. Laudner's phone-switching center. Mr. Laudner agreed to give freeconferencecall.com a "marketing fee" based on phone traffic, which amounted to splitting the per-minute access fees roughly 50-50 for each call.

In the summer of 2005 Mr. Laudner filed standard paperwork with regulators to justify his 5.3-cents-a-minute rate by presenting evidence of his past history of handling very little phone traffic. At the time, it was unclear how dramatically the traffic would jump. The FCC as well as AT&T reviewed his filing and didn't protest.

"We were taking the rules the way the rules were intended," says Mr. Laudner. "I didn't know how much traffic I was going to get."

Several weeks later after a few technical hiccups Mr. Laudner got the system up and running at full speed. Calls to his exchanges were slowly escalating as word spread online about the services.

The big phone companies didn't initially notice the impact of Mr. Laudner and Mr. Erickson's deal.

Mr. Erickson traveled to a barbecue in Iowa to meet Mr. Laudner face to face and to try to pick up more recruits. The two men ate ribs and played a round of golf.

During this period, Mr. Laudner struck partnerships with three other conference-calling firms. Suddenly, Farmers Telephone of Riceville was processing millions of minutes of phone calls a month, earning Mr. Laudner -- and the free-calling-service companies -- hundreds of thousands of dollars in new revenue. In November 2006, Mr. Laudner's company handled 27.4 million minutes of calls, more than double the number he had processed in an entire year before he partnered with the Internet companies. AT&T traffic alone on Farmers' network spiked to 15 million minutes in December 2006 from 121,000 minutes in January of the previous year.

The same thing was happening at nearly a dozen other small Iowa phone companies that were partnering with freeconferencecall.com and other companies, processing calls for everything from an Amish conference-calling service to "Free Phone Chat," a place where callers could "meet new friends and lovers."

About the same time in Denver, at the corporate headquarters of **Qwest Communications International Inc.**, the company's analysts began to notice a spike in the bills owed to Iowa companies. Qwest's Lisa Hensley Eckert, who reviews traffic between phone carriers, received call records from the Iowa phone companies so she could examine the jump in volume. She started plugging popular Iowa phone numbers into a search engine tracking several to Web sites such as hotlivesexchat.com, allfreecalls.net, freecalls2theworld.com.

"They all used the same three Iowa area codes," says Ms. Hensley Eckert. "To see millions of dollars going out the door -- it was much larger than anything we'd seen before."

AT&T, Verizon, **Sprint Nextel Corp.** and other phone companies were also taking note. In late 2006, Qwest and AT&T disputed their unusually high monthly bills and stopped paying Mr. Laudner. On Jan. 29, AT&T sued Farmers and three other Iowa companies in U.S. District Court there; Qwest and Sprint soon followed with similar lawsuits and filings to the FCC. In one filing, AT&T complained that the Iowa companies "make a mockery" of the system designed to compensate carriers for providing phone service in rural areas.

The charges to Iowa companies, including Farmers Telephone, affected Qwest's 2006 fourth-quarter earnings, and cost the company roughly \$10 million to \$15 million out of total profits for that quarter of \$194 million.

According to phone-company records, Riceville handled nearly 2.1 million minutes in January alone of calls to Male Box as well as five million from the Chicago Blade and Chicago Alibi, which offer adult chat and a "live personals" service where callers record and select personal ads.

Mr. Laudner says sex calls made up a sliver of his business. Most of the traffic Farmers Telephone handled came from sports chat clubs, businesses and charities including a domestic-violence prevention group, he says.

Still, word got around about the sex-related traffic. It didn't go over well in Riceville, population 900, which touts its "safe environment for children" on its Web site. A resident stopped one of Mr. Laudner's workers early this year to ask whether his company was involved in the sex-call business.

In March, Mr. Laudner received a call from [freeconferencecall.com](http://freeconferencecall.com) saying customers' calls weren't going through.

[Freeconferencecall.com](http://Freeconferencecall.com) initially blamed Mr. Laudner for the problems, and he checked his equipment, which he found to be working properly. Quickly Mr. Erickson learned the problem was more widespread than Farmers Telephone. Qwest had suddenly stopped routing some Iowa traffic through its network. And AT&T started blocking calls to numbers it tied to "unscrupulous carriers," the company says. The tactics in some cases affected regular phone traffic to Iowa, the Iowa carriers say.

Angry [freeconferencecall.com](http://freeconferencecall.com) customers who couldn't dial into their conference calls complained to Mr. Erickson, and some of them never returned to the site, he said.

"It was like stepping on somebody's oxygen hose," says Mr. Erickson who thinks the blocking was "criminal."

Mr. Laudner and other Iowa carriers were outraged. In April, he and Mr. Erickson and other Iowa phone executives, traveled to Washington, D.C., to complain about the blocking to officials at the FCC, which has in the past levied fines for similar acts.

The FCC didn't fine the phone companies but staffers phoned AT&T, Qwest, Sprint Nextel, Verizon and Embarq Corp., formerly the local phone division of Sprint Nextel, to warn them that blocking was unacceptable, according to FCC and phone company officials. In June, the agency formally barred the big phone companies from blocking the calls.

For now, despite the FCC's proposed rules, which say some of the carriers are "engaging in an unreasonable practice," the calls continue to flow to Iowa. But AT&T, Verizon and Sprint aren't paying the fees to Mr. Laudner for the disputed calls. Mr. Laudner says he is owed at least \$20 million by various carriers.

Mr. Laudner couldn't pay the free-calling-service companies their share. Farmers Telephone and freeconferencecall.com ended their relationship in late June when the companies' two-year contract expired. "Ron had been a good guy," Mr. Erickson said. "He wasn't going to go further with it and I wasn't going to try." He says he's since found other companies in nearby states to handle the calls, noting: "I don't need Iowa to do this."

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